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PRESENTATION

Operator

Ladies and gentlemen, welcome to the Swedish Match Q4 Report 2020. (Operator Instructions)

Today, I'm pleased to present Emmett Harrison, Senior Vice President, Investor Relations. Please begin your meeting.

Emmett Harrison - Swedish Match AB (publ) - SVP of IR & Corporate Sustainability

Thank you. This is the Swedish Match Full Year 2020 Telephone Conference. And with me today are Lars Dahlgren, our President and CEO; and Anders Larsson, our CFO. In the Investors section of our swedishmatch.com website, you'll find the presentation for today's call, which is intended to be viewed in conjunction with our prepared commentary, so we encourage you to follow along with that presentation. After our prepared commentary, we will be taking questions.

During today's call, there may be certain comments that constitute forward-looking statements and are subject to risks and uncertainties. Management believes that these statements are based on reasonable assumptions but can give no assurance that expectations will be achieved. Risk factors are outlined in the latest interim report and annual report, which are available on our website. Swedish Match assumes no obligation to update information concerning its expectations. A recording of this call will be made available on the Swedish Match website.

Side 3 of this presentation reiterates the headline bullets from our interim report released this morning, and we refer you to the report rather than repeating them on this call. Sides 4 and 5 are also included for your reference, with Side 4 illustrating the growing importance of our Smokefree products segment and Side 5 showing the geographic split for each of our product segments as well as the group.

With that, I will hand over to Lars, who will begin on Side 6.

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

Thank you, Emmett. The fourth quarter proved to be a strong finish to what has been an impressive 2020. The Swedish krona strengthened versus the U.S. dollar and other currencies. So our reported fourth quarter results somewhat masks the profit growth of more than 20% in both our Smokefree and Cigar products segment.

The financial performance in both the fourth quarter and full year will not have been possible without the remarkable and diligent efforts of our dedicated employees, ensuring that our consumers continue to have access to the Swedish Match brands that they enjoy. While changes to consumer behavior, travel restrictions and other governmental actions brought on by the pandemic have impacted volumes as well as planned activities for 2020, we have remained vigilant in complying with COVID-19 regulations and protocols and in pursuing market opportunities that present themselves in the market in which we compete.

Turning to the operational and financial developments of our product segments during the quarter. We have summarized some of the most notable highlights on Slide 6. ZYN in the U.S. continue to drive sales and operating profit growth for our Smokefree segment, but Scandinavia also performed well on an underlying basis. In our Cigars segment, we had another very strong quarter for our HTL varieties. And we were particularly pleased to note the progress in our Dominican facility in further adjusting to the new operating environment with COVID-19-related precautionary measures implemented.

On an underlying basis, our Lights businesses have delivered solid results over the course of the year, and on a full year basis, matches, in particular, improved its performance markedly versus the prior year.

This past year also proved to be very active -- an active year on the regulatory front. At the core of our regulatory strategy is a firm belief that consumers and societies are better off when properly informed about the health effects of our smokefree products relative to cigarettes and that attractive low-risk products that appeal to broader parts of the cigarette smoking population is a critical prerequisite for harm reduction to be effective on a wider scale. In the U.S., the adoption of ZYN nicotine pouches by smokers is evidence of this point, and we were pleased to be the first company to have filed its PMTA applications for nicotine pouches with the FDA in March of 2020.

Our cigar operations also engaged extensively with the FDA during the year as SE applications were filed for our entire cigar portfolio. In Europe, the regulatory environment for smokefree products remains underdeveloped at best and counterproductive at worst. Swedish Match remains a strong advocate for responsible, proportionate and harmonized product and marketing regulation and considers the current regulatory situation in Europe unsustainable.

Turning to the next slide. We also made good progress on the growth fronts with regards to sustainability in 2020. And I think it's quite evident that we are firmly committed to improving public health, given our investments in our smokefree businesses and the establishment of ZYN nicotine pouches as the largest single brand of nicotine pouches on the U.S. market and in the world. I also would like to highlight another key area where we took important steps during this past year, greenhouse gas emissions. Our 2020 science-based target with a reduction of 12% from 2017 levels was not achieved despite the significant improvement per unit of sales.

However, in 2020, we started to note tangible results from several of the initiatives that we have worked on for some time, particularly from our engagement with suppliers. And in the past year alone, the reduction was 7% versus the prior year despite the impressive growth of our business. Our growth ambitions remain intact, but we raised our CO2 reduction targets for the coming years to reflect our commitment to the science-based targets and the Paris Agreement.

On Slides 8 and 9, we have provided the most important drivers for the financial development of the Smokefree product segment. With stellar growth over the year, ZYN nicotine pouches now contribute with the majority of the sales and earnings in our U.S. smokefree business. During the fourth quarter, Swedish Match has seen continued increases in store velocities, maintained excellent store visibility and also expanded distribution somewhat. Year-on-year growth was impressive. And the slight sequential declines in shipments relative to the third quarter should be seen against the background of the temporary inventory build at a major distributor towards the end of Q3 as well as normal seasonal fluctuations that we typically see in the U.S. with one attributing factor being fewer shipping days in Q4.

On the ZYN marketing side, the organization has been creative in managing challenges related to the COVID-19 situation, and we are pleased that we could increase investment levels relative to previous quarters and look forward to further stepping up our activities in 2021. On the competitive side, we have seen a further ramp up during the fourth quarter with relatively aggressive distribution builds as well as the continuation of deep price promotions in selected markets and chains.

For Scandinavia smokefree, there were several unusual factors that impacted the reported performance. Similar to the second and third quarters, travel restrictions negatively impacted overall shipments but also elevated domestic Norwegian shipments. However, in December, shipments to Norway declined significantly as the trade and distributors destocked ahead of the January excise tax cuts. In January of this year, as expected, inventories in Norway were replenished.

Similar to the preceding quarters in 2020, on an underlying basis, Scandinavia smokefree generated increased operating profit relative to the prior year during Q4. For moist snuff, the volume shipment decline in the fourth quarter is not representative of our performance, and we remain very pleased with Longhorn's progression, both from a share and profitability perspective.

For chewing tobacco, 2020 has been a year of unusually resilient consumer demand. And also in the fourth quarter, Swedish Match delivered increased operating profit despite slight declines in shipment volumes, impacted by timing. Longer term, we consider other markets outside of the U.S. and Scandinavia to represent an important growth opportunity for the company. Anders will now provide some further details on the smokefree performance, starting with ZYN in the U.S.

Anders Larsson - Swedish Match AB (publ) - CFO & Senior VP of Group Finance

Thank you, Lars. Slide 10 is included for reference and illustrates the impressive growth trajectory for ZYN on a 12-month rolling basis. Slide 11 provides more details on the category development and market shares based on MSA data that captures shipments from distributors to the trade. Given the increased attention from competitors on the nicotine pouch category, it is encouraging to note the resilient market share foreseen in the fourth quarter.

But given the gradual ramp-up in competitive activity, when we look forward, we expect to see both an acceleration in consumer awareness and adoption of nicotine pouches as well as some share pressure for Swedish Match as competitors continue to build distribution and manufacturing capacity.

Slide 12 illustrates the great potential for the nicotine pouch category in offering adult cigarette smokers a viable and satisfying alternative. The adoption speed is rapid and the trajectory in the West, where the category has been gradually established over the course of the past 4-plus years, provides a clear indication of both the commercial and harm reduction potential.

On that point, findings from some relatively recent consumer studies have been enlightening. While we are still gaining a large share of our user base from moist snuff consumers, it appears now that an even larger share is coming from people who smoked or used vaping products in the last 12 months. Also encouraging, the data confirmed that consumer interest in ZYN is virtually nonexistent among nontobacco or nonnicotine users.

Turning to some details for Scandinavia and Slide 13. Despite the COVID-19 situation, the smokefree category continued to demonstrate healthy growth in the fourth quarter, and Swedish Match estimates the Scandinavian consumption, including Finnish consumption, to be up by close to 4% for the full year despite the restrictions faced by Fins. Across markets, nicotine pouches drove the growth, and Denmark was the fastest-growing market in the region with a consumption that is estimated to have tripled during the year and now amounts to about 15 million cans.

On Slide 14, we illustrate share developments within the Scandinavian smokefree market as reported by ACNielsen. Swedish Match's Q4 market share declined marginally by 0.3 points of a share point on a sequential basis relative to the third quarter and by close to 3 points on a full year basis, demonstrating the importance of our objective to improve the shared trajectory within the fast-growing nicotine pouch segment as most of the decline is attributable to a changed segment mix.

For snus specifically, depicted on Slide 15, Swedish Match continued its positive trajectory in the fourth quarter with further sequential share gains driven by the strong performance in Norway. Slide 16 shows the market share for Swedish Match within nicotine pouches and this segment share of the overall market according to Nielsen. While the recent trend for Swedish Match's market share within nicotine pouches has been more stable with sequential share gains in both Norway and Denmark, we are far from satisfied with the absolute level and the full year performance.

Turning to Slide 17 and the U.S. Our moist snuff business delivered on several important strategic objectives during 2020. Our Longhorn franchise continued to gain strength and appreciation among both retailers and consumers as its simplified pricing and promotional structure helped to further enhance brand equity. The moist snuff category showed good growth in 2020, likely impacted by COVID-19 effects on consumption patterns, and Longhorn alone represented a very respectable share of the overall category volume growth. Pouches continued to outpace traditional loose formats in terms of growth, and over the past several years, Swedish Match has been successful in achieving its goals of gaining share within this attractive segment.

For chewing tobacco, the COVID-related impact on consumer demand is quite notable as the flat category development for 2020, as depicted on Slide 18, stands in stark contrast to the historical trend of declining volumes of around 6%. Similar to previous years, Swedish Match successfully realized a positive price/mix effect on its portfolio despite continued growth of the value price segment, as depicted on Slide 19.

During the fourth quarter, Swedish Match gained share within the value segment, but lost share in the premium segment. Given Swedish Match's portfolio weighting to the premium segment, the growth of the value price segment resulted in a slight overall share erosion for Swedish Match. For the full year, with share gains within both the premium and value price segments, Swedish Match's share within the overall category was stable despite shift in segment mix.

We will end this smokefree part of the presentation with Slide 20 providing a snapshot of new products, packaging and markets, which we have launched over the past year for snus and nicotine pouches. Despite the challenges brought on by COVID-19, our dedicated product development, supply chain and sales and marketing organizations have continually adopt -- adapted to provide consumers with new and upgraded offerings across our markets, and we look forward to another active year in 2021.

Turning to our next largest product segment, Cigars, on Slide 21. Our strategic objective for our Cigar product segment is to maximize long-term profitability and cash generation. Through our approach, we have been able to record operating earnings growth and market share gains by participating in the overall growth of the category by benefiting from the consistent migration of consumer preferences away from HTL to natural leaf cigars and by increasing list prices when market dynamics allow. With COVID-19 impacts on consumer demand as well as challenges in our supply chain for natural leaf cigars, 2020 has been an unusual year.

Category growth was very strong, but Swedish Match's ability to fully participate in the growth of the natural leaf segment was hampered by COVID-related production constraints at our Dominican facility, most notably in the second and third quarters. Production of natural leaf cigars has reverted to pre-COVID levels in the fourth quarter of 2020, and we experienced market share growth within the natural leaf segment toward the tail end of the fourth quarter. Our ability to manufacture HTL cigars at our U.S.-based facility helped to migrate our -- mitigate our natural leaf production shortages, resulting in an impressive increase in shipment volumes of HTL varieties.

It should be noted that while not representing a significant part of our overall portfolio, we took consumer prices up on our value-priced offering jackpot during the fourth quarter from 3 for \$0.99 to 3 for \$1.19. In addition, we announced a price increase to the factory selling price of our White Owl HTL cigars in January 2021 of \$0.01 per stick, the full benefit of which will not be realized due to increased federal excise taxes on the price increase. Pricing continues to represent a significant potential earnings driver in a category that has not experienced much in the way of consumer price inflation in the past 5 to 10 years.

Slide 22 illustrates the acceleration in volume growth that we experienced over the course of 2020 as well as the dynamics behind our overall market share gain for the year. Despite the pickup in share within natural leaf late in the fourth quarter, Swedish Match's share within that segment was lower than in 2019 on both a fourth quarter and full year basis. But with the impressive performance during the year of our HTL varieties, overall market share ended on a higher level in 2020 than in 2019.

Side 23 illustrates the composition of our cigar portfolio by type of cigar, demonstrating our continued tilt towards the faster-growing natural leaf segment despite the supply chain issues experienced in 2020. Moving on to Side 24 and our Lights product segment. The Lights segment delivered another good quarterly result on an underlying basis. And while the reported numbers for the year 2020 and 2019 both were impacted by income of onetime character, including capital gains related to our asset realization program in Brazil, the underlying results for both lighters and matches have been consistently good over the course of 2020.

Match volumes grew in 2020, largely attributable to solid performance in the important Brazilian market. And while lighter volumes were down for the full year, impacted by COVID-19-related restrictions, the fourth quarter reverted to volume growth, delivering the strongest volume performance of the year, coupled with a good mix. In addition, complementary products in Brazil continued to generate strong growth in local currency for the year.

On the regulatory front. On Side 25, we have summarized the more notable regulatory events which have occurred during the fourth quarter. In California, the flavor ban for tobacco products, which also included a state-wide ban of flavors for nicotine pouches, has been suspended at least until after a referendum in November of 2022. Swedish Match's nonflavored offerings of ZYN are already available in California, and ZYN with 4 new flavored SKUs in popular nicotine strengths is well positioned in the event of a flavor ban versus the other larger nicotine pouch competitors. In Norway, it is encouraging that the authorities may have considered the difference in the risk profile in their decision to cut the tax on snus but not for cigarettes. In Germany, a number of local authorities, referring to food regulations, have imposed sales bans on nicotine pouches. And while these decisions have been appealed, Swedish Match has halted sales pending legal review.

On Side 26, we have summarized relevant metrics for our interim report relating to finance costs, our financial position and earnings per share. Net finance costs during the quarter were in line with the levels that we experienced during the past few quarters, bearing in mind the onetime charge during the third quarter related to the adverse ruling in an ongoing tax case. The weighted average interest rate of our loan portfolio at December 31 was 2.07% compared to 2.08% at the end of 2019. In December, we did a tap issue of EUR50 million on our existing 2025 bond with an all-in fixed interest rate in Swedish kroner of 1.4%. In January 2021, we repaid SEK 750 million of debt and an additional SEK 1.1 billion will be repaid during the third quarter. The weighted interest rate on these repayments is notably lower than the current weighted average of our loan portfolio. The capital duration at year-end was 3.7 years with 98% of the bond portfolio subject to fixed interest rates.

The EPS bridge illustrates the components of our 27% full year growth in adjusted EPS. The adjustment highlighted in the EPS bridge refers to the tax expense and interest, in total SEK 286 million related to the mentioned adverse Swedish tax ruling. While we funded the full amount of the judgment during the third quarter, we continue to believe that our position is justified and a leave to appeal has been filed with the Supreme Administrative Court in Sweden. During 2020, we made share repurchases in the amount of SEK 3.1 billion, which means that this year SEK 5.1 billion has been returned to our shareholders via share repurchases and dividends.

Side 27 restates our 2021 outlook from the interim report. And on the point of expected negative translation effects, you may want to take note of some of the more important average exchange rates versus the SEK. The average exchange rate in the first quarter of 2020 for the U.S. dollar was 9.67, the NOK 1.02 and the Brazilian real 2.80.

And with that, operator, please open up the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Niklas Ekman from Carnegie.

Niklas Ekman - Carnegie Investment Bank AB, Research Division - Head of Consumer Discretionary & Staples and Financial Analyst

Just a couple of questions, if I may. Firstly, on ZYN, if you could comment a bit on the competitive environment. There's been a lot of talk about drift BAT having accelerated its rollout recently. You mentioned this on the call here as well on Altria. Can you just elaborate a little bit on how their capacity constraints compare to you, the store rollout, store availability, how that compares to ZYN? Just an indication here would be very interesting, please.

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

Yes. I mean, first of all, and this is Lars here, you should, of course, speak to them on the specific details. But what we do note is a rather significant increase in distribution during the fourth quarter, especially towards the tail end of the fourth quarter when we talk about BAT and what's now Velo, which effectively was the drift product. And in terms of capacity, there we rely on what they communicate and what you read, where Altria, as you probably know, speak about an annualized capacity of 50 million cans by now, but removing capacity constraints going forward. While we haven't seen any specific communication on capacity for BAT, but you would assume that they have installed capacity or invested in capacity to be able to cater to the increased distribution that they are driving right now. And they are relatively aggressive also when it comes to offers to the consumers. And whether this is temporary, so to say, trial offers or not, that remains to be seen. But consumer prices down to \$0.99 per can, et cetera, are relatively frequent.

Niklas Ekman - Carnegie Investment Bank AB, Research Division - Head of Consumer Discretionary & Staples and Financial Analyst

And have you (inaudible) into that at all (inaudible) manufacturers take around \$3?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

Sorry, your line was severely cut there, but I heard...

Niklas Ekman - Carnegie Investment Bank AB, Research Division - Head of Consumer Discretionary & Staples and Financial Analyst

Sorry about that. Just a question if you had responded to that? Or are you sticking to around \$3 per can in manufacturers take (inaudible)?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

Our Q4 net take is close to \$3. So we have continued to have a relatively limited promotion as of this stage.

Niklas Ekman - Carnegie Investment Bank AB, Research Division - Head of Consumer Discretionary & Staples and Financial Analyst

Excellent. Just also a general question on the underlying market for smokefree products. How much – of the nicotine pouches, how much of this growth has been at the expense of moist snuff, how much do you think is incremental and mainly at the expense of cigarettes? If you could just elaborate on kind of the long-term trends you're seeing.

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

I mean I think we need longer data periods to be able to give more accurate answers to those type of questions, especially in a year like 2020, impacted by COVID. So we did see a category growth of around 3% in moist snuff. We continue to note that the relative performance within the moist snuff category was the weakest in the Western region where the nicotine parts category is most developed. I mean official cigarette numbers don't really indicate any detectable impact from nicotine pouches per se. But at the same time, as Anders explained, our consumer research suggests that when we previously have been talking about half of the consumers being sourced from smokefree and half from other, most notably cigarettes

and vape products, there are indications in the latest round of research that the share of consumers coming from cigarettes and vape may be a bit more than 50% for (inaudible).

Niklas Ekman - Carnegie Investment Bank AB, Research Division - Head of Consumer Discretionary & Staples and Financial Analyst

Okay. And (inaudible) are you following your competitors? Or are you leading price hikes?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

I didn't hear the first part of your question, but we don't comment on future pricing activities.

Niklas Ekman - Carnegie Investment Bank AB, Research Division - Head of Consumer Discretionary & Staples and Financial Analyst

Sorry, the question was, if you were the first to raise prices in cigars or if you were following your competitors?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

I mean, if you take the jackpot brand there, one of our competitors, at least, have been fairly inactive in that segment, which is something that may be related to production constraints. So in that sense, we were leading, you can say.

Operator

And the next question comes from the line of Richard Felton from Goldman Sachs.

Richard Felton - Goldman Sachs Group, Inc., Research Division - Equity Analyst

Two from me. So the first one is on Slide 12, where you've changed your slide slightly and now show nicotine pouches compared to the cigarette category, where previously you were showing it compared to moist snuff. Does a change in this slide and some of your comments about the consumer research that you've been doing, should we interpret that as the way that you're thinking about this opportunity -- or the opportunity for nicotine pouches in the U.S. slightly differently to previously? And then related to that, the 4% versus the cigarette category that you've achieved in the Western region, is that a reasonable benchmark for what you think that the nicotine pouches category can achieve nationally? And what do the consumer surveys that you've referenced suggest as a plausible target? That's my first question.

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

Yes. Thanks for that question. When it comes to these nicotine -- or sorry, moist snuff benchmarks, if you listen to our calls over the past years, so we've been we've been pointing out that we have provided these benchmarks to give a good reference point for the size of the category, but recognizing that consumers are also, to a large degree, sourced from not the leaf cigarettes.

And our view is and continues to be and further strengthened by recent consumer research that we expect to see the share of, sort of say, cigarette smokers and vapers a share of the inflow to the nicotine pouch category to increase over time as the category becomes more established in the broader parts of the population. So yes, I would say that it is more relevant, we think, to view the size of the U.S. cigarette market as an indication of the long-term potential.

And we know from our experience in Scandinavia that once you really find, so to say, satisfying alternatives that reaches beyond niche acceptance in -- among consumers that firmly become established. And the potential relative to cigarettes is very big, and as you know, in Sweden, Norway,

it's actually even surpassed cigarettes. On the second part of your question, generally, we see -- when we look at velocity levels, so far, we continue to see similar trajectory in the so-called expansion markets compared to what we saw in the West. And so from that point of view, a conclusion could be that 4% after a similar amount of time in the expansion market could be a reasonable estimate of how the category will develop. However, having said that, there are reasons why it could be both stronger and weaker than that.

Stronger, one reason clearly is that, first of all, the Western region, you should remember, has been, so to say, established over time. And I think it's fair to characterize the Western region as relatively fully in distribution now, but that hasn't been the case over the entire 4-year period. And also, we have a completely different competitive situation now in the expansion markets compared to what was the situation in the West when the category was established and built that could speak for even a faster adoption. However, there may be differences in consumer preferences to the extent that for those that are coming from moist snuff and so forth.

So you -- when you look in the rest of the country, you will market the product in more states with relatively low taxation on smokeless products, meaning that the price difference may be more notable between nicotine pouches and moist snuff. And then of course, there are other alternatives being marketed and developed. So we expect our competitors not only to focus on nicotine pouches, but also on other next-generation products in their portfolio. Sorry for the long answer.

Richard Felton - Goldman Sachs Group, Inc., Research Division - Equity Analyst

Appreciate the color. And just one follow-up, if I may, on cigars, where profitability was very strong in the second half. And I appreciate some of that boost is from operating leverage and temporary COVID factors, but also some positive mix within your HTL portfolio and some of the pricing that you referenced. Can you maybe help us understand and quantify those factors? And maybe how we should think about margins for cigars in FY'21?

Anders Larsson - Swedish Match AB (publ) - CFO & Senior VP of Group Finance

Anders here. You're right that -- I mean we have seen efficiency gains from our HTL production over the course of this year. And then, of course, given the COVID situation, it's a bit tricky to foresee how that will play out over the course of this year, but we are happy with the performance. And hopefully, we can continue to benefit from those efficiency gains throughout this year and -- while also growing within natural leaf, which is still our aim for '21.

Operator

And the next question comes from the line of Andreas Lundberg from SEB.

Andreas Lundberg - SEB, Research Division - Analyst

If I move to Scandinavia, I think you reported some snus shipment volumes down 9% year-on-year. Could you perhaps provide a little more color on dynamics of this decline when it comes to COVID, Norway, Finnish consumption, et cetera? That's my first question.

Anders Larsson - Swedish Match AB (publ) - CFO & Senior VP of Group Finance

Andreas, Anders here. Yes, there was a quite steep decline in the fourth quarter and a big piece of that is destocking effect ahead of the Norwegian tax decrease in January of this year, which was quite notable, I think. It's fair to assume that, that was an impact of around 3 million cans, which has come back from what we see in January now. So I think if you adjust for that factor, you get a better sense of the underlying performance in, so to say, a COVID environment with all the mix effects going on last year and continue to do so this year.

Andreas Lundberg - SEB, Research Division - Analyst

I understand. And then on Norway and the tax reductions, could you say anything about what that has meant for the category here when it comes to, for instance, manufacture pricing positioning for certain products at the start of 2021?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

It's a pure tax change and it's a weight-based tax in Norway. There you can say there is an ad valorem component because there is VAT on the excise tax, but it varies a little bit from chain to chain. But generally, largely the Norwegian trade has adjusted its price is in line with the tax decrease, including the VAT effect. And on the Swedish Match side, we have done it similar. And we had already, before the tax cut was decided, communicated to our trade, our sort of what has at least historically been annual, what I would call, normal inflation level-type price increases. So nothing different in that respect on the manufacturing side for Swedish Match, at least.

Andreas Lundberg - SEB, Research Division - Analyst

Okay. And that goes for all your products? Or has anything changed internally between various products of the markets?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

I mean there can be slight differences within the portfolio, but generally, that is the case.

Operator

And the next question comes from the line of Faham Baig from Crédit Suisse.

Mirza Faham Ali Baig - Crédit Suisse AG, Research Division - Research Analyst

I've got 3 on ZYN, if that's okay. Firstly, your market share seems to be holding up extraordinary really well despite you mentioning competition increasing price promotion and also distribution. Could you maybe suggest why that might be and why you believe ZYN is holding up so well? And related to that, you highlighted you stepped up marketing investment in Q4 and you're going to do a further step-up in '21. Could you help us give some quantification of what that marketing step-up might look like? I note your margins in ZYN, for example, in Q4 were about 55%, if I've done my math correctly. And any comment on margin potentially for ZYN in '21 might be a helpful indication for us to understand that a bit more. And the final question I have on ZYN is, as you mentioned, competition talking about capacity and no longer being constrained in '21.

Could you please give us an update on where your capacity lies for '21, when you're likely to be no longer under constraint? And then slightly related to that, I believe your current CapEx plans are such that you're targeting around 240 million cans as a run rate for '21. Could you just remind us of your plan beyond '21 and going into '22 and thereafter, please?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

If I -- a comment on the market share. As we said in the prepared commentary, we are very pleased with the resilience during the fourth quarter. We did see that one of the big competitors was particularly active in the third quarter with price promotions. And while still ZYN in the market from that particular competitor have been scaled down a bit and encouraging to note is that ZYN then post promotion picked up its share in several chains. And then we've seen towards the tail end of the quarter, an impact -- or an increase in both distribution and promotional activity from the other large player. And the word tail end there is important because you look at the full 13-week period on that slide in the presentation.

So we should expect that with that type of distribution build and promotional pricing, that January market shares will look notably different. But what's important, of course, is what's happened -- happening longer term, and we remain convinced that we have a very attractive portfolio that stand very well versus competition.

Anders Larsson - Swedish Match AB (publ) - CFO & Senior VP of Group Finance

Yes. And on your second question, Anders here, relating to marketing spend, I don't want to disclose the marketing budget for our U.S. operations. But obviously, we do, as also indicated in the outlook, expect to spend more on marketing initiatives. And obviously, when you add incremental spending without adding corresponding volumes, that will have an impact on margin. And I think it's fair to assume that it will also increase on a per can basis for '21. I think that is about what I can say on that point.

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

And specifically between the third and the fourth quarters, as Anders said, we did increase spending on the marketing side, which is very positive that we managed to activate and build the brand more, so to say, despite the COVID environment. And then you need to factor in also that in a high gross margin category like nicotine pouches for Swedish Match, of course, those type of volume impact when you have a lower volume, that is also seen in -- on the margin side from absorption effects and so forth. And on your question on capacity, we are right now in the midst of starting machinery, so to say, line by line, as we speak in this third phase, which is doubling of the capacity compared to what we had installed before, and it's going very well. And then we have taken further investment decision, as you referred to, including buildings, expansions and so forth. But now it's going so well. So we don't disclose specifically what we think we can manufacture this year.

I think the important take is that we are kind of over the hill now where we feel that capacity -- production capacity will not be the constraining parameter for how much nicotine pouches we will sell in the U.S. market going forward. And we intend to make sure with hopefully continued investment decisions that is going to stay that way.

Mirza Faham Ali Baig - Crédit Suisse AG, Research Division - Research Analyst

Brilliant. If I could squeeze one more question in just related to ZYN. Q4 saw -- if I look at the underlying trends in Q4 for ZYN, taking into account the 3 fewer shipping days as well as the inventory adjustments, you still did see a sequential slowdown in the category's growth. Would you expect that underlying growth momentum to increase in 2021 and in Q1 as those capacity constraints are no longer visible and you've got a step-up from competition and investing behind the category as well?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

I think longer term, we expect the focus on nicotine pouches in the market to be very positive for the adoption of the product among consumers. Then the type of very steep increases that we have seen in our portfolio from the West where we came from a very, very high market share, now when, so to say, there is more to be shared in the rest of the countries. So although the category may be following the West, that could imply a slower sequential growth for Swedish Match if we are right in our assumption that the category will continue to grow very well, but we will see a bit of pressure on the marketing side. And when we look at the velocities in the category in Q4, their MSA data did indicate a relatively nonexistent sequential growth in the fourth quarter in the Western region. But we wouldn't read too much into this in this short period, actually, because it is -- first of all, it's always difficult around year-end. So you're comparing a year-end 13-week to a preceding 13-week. And we did actually note a bit of destocking in California, which is a relatively large part of the Western region ahead of the -- what could have been the flavor ban in that market.

Operator

And the next question comes from the line of Gaurav Jain from Barclays.

Gaurav Jain - Barclays Bank PLC, Research Division - Research Analyst

I have a few questions just following up on what you just said on the destocking. So look, you had 3 fewer shipping days, which anyway would have led to lower inventories at distributors, and then you are saying there is a further inventory drawdown. So how do I triangulate that? And if I look at Q1 '21 because it will have 3 extra shipping this, does it mean that sequentially just what you report would have a much higher growth?

Anders Larsson - Swedish Match AB (publ) - CFO & Senior VP of Group Finance

So Anders here. I didn't follow exactly your math there on the growth. But I mean, when we see -- what we said in the third quarter was that we had 3 extra delivery days versus the fourth quarter, and then we have another I think it's 2 extra versus the fourth quarter now coming in the first quarter. And then the distributor load that we had in the third quarter was kind of a one-off for the third quarter.

Gaurav Jain - Barclays Bank PLC, Research Division - Research Analyst

Sure. Okay. And maybe I can follow this up separately, what will be the shipping days every quarter. But what I'm trying to understand is that because of fewer shipping days, anyway inventory would be lower at wholesalers, so why would you have a further inventory drawdown compared to what you are highlighting? Because I guess the question is that is there a risk that the inventory drawdowns are sort of forecasting or suggesting a real slowdown (inaudible)...

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

Normally, it is difficult to have the same kind of shipping days as the manufacturers. So the distributors have a similar pattern to the trade.

Emmett Harrison - Swedish Match AB (publ) - SVP of IR & Corporate Sustainability

Yes, it's not uncommon to see some drawdowns at the retailer and distributor level during the -- you could say, the holiday period, kind of November, December, that's not uncommon. You see it in -- 2 in tobacco, moist snuff, in several of the categories that we have, where there's a natural drawdown. The 2 unusual ones when it comes to some reductions are in California, where there was some -- perhaps some drawdowns with the thinking that the flavor varieties would not be there. That's one. And the other one was this major distributor having increased inventories in the third quarter having reverted back. And that's what gives you that 2-plus million cans, 2 million to 3 million can shipped between Q3 and Q4. So one is more of an isolated distributor effect and the other one is an isolated state effect. And then the fewer shipping days or the fewer days during the holiday season and so forth corresponds to kind of a normal event if you look at Q4 this year versus Q4 last year. It was really Q3 versus Q4 that we wanted to make sure we highlighted.

Gaurav Jain - Barclays Bank PLC, Research Division - Research Analyst

Sure. That's very clear. Now my second question is on the losses in smokefree, which is outside U.S. and Scandinavia, which were much higher than Q4. In fact, they were as much as in the first 3 quarters of 2020. So which countries are you investing? And how should we model this for 2021, that is Q4 2020, the run rate for every quarter going forward?

Anders Larsson - Swedish Match AB (publ) - CFO & Senior VP of Group Finance

Yes. Anders here. I think one needs to be a bit careful of following the kind of quarterly spending here because it is it's not like we have a linear spending across the year. So it can vary quarter-by-quarter a bit, but we do expect continued investments going forward. And I think it's fair to assume that those will go up on a full year basis, but then how it will look like quarter-by-quarter is -- it's not a linear spending.

Gaurav Jain - Barclays Bank PLC, Research Division - Research Analyst

Sure. Okay. And my last question is on the U.S., 6 states are now offering MRTP-related excise tax reductions on products which have MRTP, and these number of states seems to be going up. So I'm surprised that you are not keen to file an MRTP to just take advantage of these MRTP tax breaks. So could you just help us understand why that's the case?

Emmett Harrison - Swedish Match AB (publ) - SVP of IR& Corporate Sustainability

Sure. Nicotine pouches in most states have no tax at all. So getting an MRTP for nicotine pouches really doesn't have an impact on that. One of the things that we saw when we received the MRTP for General Snus, it's a quite positive thing, but it hasn't had a really dramatic impact, any notable impact really on our overall volumes within the total market. The other thing is that when we do our pricing modeling, for our moist snuff, for our snus, for our nicotine pouches, we do it with a comparative set. So nicotine pouches often are priced in line with premium moist snuff or snus products and so forth. The nicotine pouches already have, in most states, a notable tax advantage versus other smokefree tobacco products.

Operator

And the next question comes from the line of Robert Rampton from UBS.

Robert Amos Rampton - UBS Investment Bank, Research Division - Associate Analyst

So looking at the total category, you've given us some indication of how share is evolving over Q4 and how you expect it to evolve in January. But can you give us some insight into how the category as a whole and your own product did over the quarter and early into 2021? I'm just keen to understand how that growth moves with the increases and decreases in competitive intensity. That's my first question.

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

I mean if we take the fourth quarter was -- I don't have that number in front of me what the MSA data showed, but it was similar growth in the expansion markets compared to before, but virtually 0 growth in the Western region. So on an aggregate level, it was a slowdown for the category. And then when it comes for January, that is something we need to get back to. I mean we only have a couple of data points there, and we're already into discussing very detailed data on short periods, which I think is a little bit dangerous in terms of drawing conclusions. But as a general comment, we would expect that with increased competitive activity in distribution and [building] and so forth, it is natural to expect an increased shipments out to the trade as well.

Robert Amos Rampton - UBS Investment Bank, Research Division - Associate Analyst

Great. That's very clear. Just on to the margin, can you kind of break down how much of the pressure for ZYN in Q4 was marketing? And just how -- looking at 2021, how we should think about that in the context of improved capacity, which I assume would reduce COGS per unit?

Anders Larsson - Swedish Match AB (publ) - CFO & Senior VP of Group Finance

Yes. Anders here. No, I think -- I mean, it's we don't disclose that level of detail of exactly how much was driven by marketing spending on a quarterly basis. But as mentioned, we do expect higher spending. You can expect likely some benefits from the higher volumes going forward. But then you should also remember that, I mean, with those onetime factors on shipments, with extra distributor loading in Q3 as well, that also had an effect comparing Q3 to Q4.

Robert Amos Rampton - UBS Investment Bank, Research Division - Associate Analyst

Okay. Cool. And sorry, just my last question, apologies. Just in terms of the market share evolution in the West versus the national region, could you give us an update on market shares in those 2 regions for 4Q?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

Yes. We continue to have a higher market share in the West. There seems to have been a bit of an increased focus from competition to try to make a dent into our strong franchise, but also, we've seen good -- very good resilience when competitors have come off promotions. So it is notably higher in the West compared to the rest of the country.

Robert Amos Rampton - UBS Investment Bank, Research Division - Associate Analyst

Okay. And versus previous quarters, is it better to interpret that as stable?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

I don't have the exact split on a sequential basis, Q4 versus Q3 in front of me, but I think it was similar trajectory, maybe a little bit down in the west, given where we were coming from.

Operator

And the next question comes from the line of Karri Rinta from Handelsbanken.

Karri Rinta - Handelsbanken Capital Markets AB, Research Division - Research Analyst

Sorry for continuing on the ZYN. When it comes to the U.S., if you look at the -- you comment that you are no longer capacity constrained, whereas your main competitors are, at least for the next 6 months. So wouldn't it make sense to try to establish as wide of a distribution network as possible ahead of your competitors solving their capacity constraints because besides capacity, I guess, their distribution footprint is the sort of the competitive advantage that they have given their presence in the U.S.? So is that part of your sort of marketing strategy for the first half that you really try to -- that you go all out when it comes to adding new points of sale? That's my first question.

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

I mean, as we responded on an earlier question, when it comes to exact capacities for competitors, you should ask them. In particular, in terms of VAT, we are not aware of any those numbers. I would urge you to take more of a view of, so to say, what is going to drive market share is consumer demand out there in the market rather than focusing on exact capacities month-by-month. Because I mean, most manufacturers have the ability to adjust on the short-term basis and then you have the [valve] of inventory fluctuations and so forth. And I would also do the math, if you take the competitor that speaks about 50 million cans annualized capacity, 50 million cans roughly corresponds to 30% of the category, and Swedish Match has north of 70% of the category so -- in the fourth quarter. So I'm not completely sure that it's a correct conclusion to say that competitors have been capacity constrained in that sense. But of course, it could still have impacted their distribution builds and so forth.

Karri Rinta - Handelsbanken Capital Markets AB, Research Division - Research Analyst

Okay. But I mean the question was that if we don't have to talk -- think about manufacturing capacity, how big of a competitive advantage is to have a wider distribution network or wider presence in terms of point-of-sale in the U.S.?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

I mean it's clearly an advantage to have a broader distribution. And then you want to have distribution in stores that have good velocities as well because the brands need to -- or the products need to move off the shelves and get in the hands of consumers.

Karri Rinta - Handelsbanken Capital Markets AB, Research Division - Research Analyst

All right. Then a follow-up on that. If we then look at the Scandinavia, I mean your market share in nicotine pouches is persistently low. And I mean, is that an indication of how -- I think I have probably posed this question before, but is that an indication of how important it is to be a first mover? And by that token, how worried or not worried should we be about the U.S.? Or is there something specific -- which specifics should we consider when we try to sort of compare the Scandinavian market and the U.S. market in terms of what is a realistic long-term market share for a market leader?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

I mean the first-mover advantage is a good thing in consumer goods, as you know. And then I think it's a little bit difficult to draw exact conclusions or parallels between the Scandinavian market and the U.S. market. And I mean, one, the trade structure is different and so forth, but then also a notable difference is the regulatory framework with the FDA, where you need to go through the PMTA applications to introduce new products in the U.S. market, while as in Scandinavia, that is not the case. That is still the case. As you alluded to that BAT has a very strong foothold in Scandinavia, but they've done a good job on the product and marketing side as well as distribution as well that is helping maintaining their share.

Karri Rinta - Handelsbanken Capital Markets AB, Research Division - Research Analyst

All right. And then finally, a short question on the PMTA and FDA that you mentioned. When you filed your application, what kind of guidance did you get from them in terms of how quickly they would get back to you on that, i.e., how long does it take to get it approved?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

We know that it's in review and that they are active. And we're refraining from speculating on FDA response time because it's proven very difficult in the history.

Operator

We have 1 final question from the line of Sanath Sudarsan from Morgan Stanley.

Sanath Sudarsan - Morgan Stanley, Research Division - Research Associate

Quick ones from me. First of all, coming back to Slide 12. Are you able to kind of give us some sense on how the change in consumption has happened in terms of how much is driven by distribution rollout and how much is driven by consumption increases in the existing stores? And also, what I would like to understand is what is the -- in your understanding, the peak level of consumption per user per week for this category as it stands? Secondly, I just want to understand also on the capacity front, you say you will be self sufficient. Is there a change in the way we should think about the time lag you would take to add incremental capacity? Is it now going to be a faster rollout given all the basics are in place? Or should we assume a similar lag in terms of when this capacity would come on board? And then the last 1 on Europe. I appreciate the amount of investments you've put in. But could you just run us through some of the key performance metrics, maybe stores added or consumer traction that you received in the last quarter? And what are you aiming at for 2021 along with the capacity you have to service that?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

I mean, if we -- first, on the U.S. capacity, nothing has really changed in terms of lead times, I would say, apart from that, of course, our teams get more and more experienced with installing new equipment. So what you see now is more the effect of us having taken a lot of decisions and putting that capital into action, which means that we now see that we will be able to stay ahead of the curve. When it comes to the growth and the reference to Slide 12, generally, we have seen the combination of very good velocity growth and distribution build. So it's only the later periods in the West, where we have seen a little bit more of the build coming from distribution. And while we've seen kind of velocities maturing a bit, but still showing good trends if you look over the second half of last year and at a very attractive level. And in terms of other markets, we have a small presence in several markets, and we don't disclose specifics of each market. But what we are looking, of course, at is establishing distribution in relevant chains and so forth, and we are tracking velocities and market share and overall category performance.

Sanath Sudarsan - Morgan Stanley, Research Division - Research Associate

Can you...

Anders Larsson - Swedish Match AB (publ) - CFO & Senior VP of Group Finance

And -- sorry, Anders here. Just to remind you of the negative effects from the ruling in Germany on chew bags, which has, of course, affected performance in that subsegment.

Sanath Sudarsan - Morgan Stanley, Research Division - Research Associate

Sure. Just on Europe, are you -- what's the kind of strategy we should think about? Because -- and I think as someone alluded earlier, there is clearly seemingly a first move advantage in the category. Of course, you need a great product. I'm not disputing that. But how should we think about your Europe expansion? Is it more of trying to build the category or you -- which could be very expensive? Or is it more on building on some of the platform built by your peers?

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

I mean it's relatively crowded already in the European market, but that doesn't mean that you cannot see there will be markets where Swedish Match goes in first. There have been several markets on the Balkans where that has been the case. That has been the case in Italy, but also actually, in Italy, there is a regulatory uncertainty at the moment. So right now, that -- sales to that market have been halted until we see regulatory clearance. So it's a combination, but you see a lot more products in the European market compared to the U.S. market, for example, also from small players that are not coming from the big tobacco company.

Operator

And as there are no further questions, I'll hand it back to the speakers for closing remarks.

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

Okay. Then we would like to thank everybody for listening today, and inform you that the release of our first quarter results will be on April 30. Thank you very much.

Operator

This concludes our conference call. Thank you all for attending. You may now disconnect your lines.

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